

STATE OF WISCONSIN
DEPARTMENT OF EMPLOYEE TRUST FUNDS
801 West Badger Road
Madison, WI 53702

CORRESPONDENCE MEMORANDUM

DATE: February 14, 2003

TO: Wisconsin Retirement Board
Teachers Retirement Board
Employee Trust Funds Board

FROM: Julie Reneau, Administrator
Division of Retirement Services

SUBJECT: Emergency Rule to Revise Dividend Distribution

Recommendation

The Department recommends that each Board approve an emergency rule that would return the effective date of the fixed and variable annuitant dividends in 2003 from March 1 to April 1. This would result in this year's annuity adjustments being made to the May 1 payments instead of the April 1 payments, as is currently provided by rule.

Secretary Stanchfield has statutory authority, with the approval of the Boards, to request an emergency rule under §227.24 (1) (a) Wisc. Stats.:

"An agency may promulgate a rule as an emergency rule without complying with the notice, hearing and publication requirements under this chapter if preservation of the public peace, health, safety or welfare necessitates putting the rule into effect prior to the time it would take effect if the agency complied with the procedures."

A promulgated rule under this provision takes effect upon publication in the official state newspaper and remains in effect for 150 days, unless further action is taken to extend the expiration date.

Background

The date on which the annual fixed and variable dividends are distributed to annuitants is established by administrative rule. Until October of 2002, the applicable rule specified that the effective date of the annual dividend was April 1 (reflected in the May 1 payments).

Annuitants and annuitant groups had long requested that annual dividends be early in the calendar year so that they could receive expected benefit increases as soon as possible. Improved technology made it possible for the Department to calculate and pay the annual annuitant dividends one month earlier. After discussing the pros and cons, the Department initiated a rule amendment that would change the annual dividend effective date from April 1 to March 1 (reflected in the April 1 payments).

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Based on the Department's request, the three retirement Boards approved the scope statement for the rule change at the March 2002 meetings. A public hearing was held on May 16, 2002; no one appeared at the hearing, nor was any written testimony submitted for or against the change. The Boards then approved the final rule draft at the June 2002 meetings, and the amended rule was promulgated effective October 1, 2002. Therefore, under the existing rule, this year's dividends would be effective on the April 1 annuity payments.

Discussion

The change to the administrative rule was initiated with the best of intentions, primarily to get the additional money from dividend increases into the hands of annuitants as quickly as possible. In retrospect, the timing is unfortunate. We have had three consecutive years of investment losses in both the fixed and variable funds. As a result, there will be no fixed fund annuity dividend this year, and there will be an estimated variable annuity decrease of 27% (the final variable adjustment has not yet been determined). Many annuitants are now aware that not only will there be a large variable annuity decrease, there will also be no fixed annuity increase to partially offset the variable decrease.

The continued deterioration of investment returns in the latter part of 2002 has magnified the adverse, near-term effect of this change in timing (i.e. the size of the negative variable adjustment is larger). Given the uncertain economic climate, many experts feel that investment returns will be unusually low for the foreseeable future, likely delaying the point at which positive annuity adjustments would offset the loss caused by the one-month advance. We have received inquiries from many affected annuitants and others asking us to reconsider the timing of the change.

Here are some facts for consideration and discussion:

- Brian Murphy, of Gabriel, Roeder, Smith & Co., confirmed that changing the distribution date does not affect the fixed dividend or variable adjustment for 2002.
- We currently anticipate no change in the fixed annuity amounts and a large loss (estimated -27%) in the variable annuities.
- A variable change of 27% equates to approximately \$8.5 million paid from the annuity reserve.
- There are approximately 29,000 annuitants in variable who will experience an average monthly drop of \$297 in the variable portion of their annuities (in addition to the effect of the negative 11% and negative 14% variable adjustments in the past two years).
- The extremely poor economic climate is affecting all of our annuitants in other ways as well (personal savings dwindling, etc.).
- The emergency rule stays in effect for 150 days. After that, administrative code reverts back to the prior permanent rule, unless changed.

Summary

Due the financial harm that the current administrative rule will create for variable annuitants, at least in the near future, the Department proposes an emergency rule that would change the 2003 annuity dividend effective date from March 1 back to April 1. This does not change the existing rule permanently, unless further action is taken to amend the permanent rule before the 2004 annuity dividends are distributed. However, the emergency rule (effective for 150 days) eliminates the additional harm that the earlier distribution date will create this year, and will give the Department an opportunity to evaluate and recommend a long-term solution to the Boards at a later date.